

An Overview of Value Added Tax (VAT)

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AN OVERVIEW OF VAT

AREAS TO BE COVERED IN THIS HOUR

- A. VAT Implementation Plan**
- B. Economic Significance of VAT**
- C. Salient features – Federal VAT Bill**
- D. Salient features – Provincial VAT Bill**
- E. Implementation Issues**
- F. Administrative Action Planned & in Progress**
- G. Way Forward**

A. VAT Implementation Plan – I

1. The new VAT Acts will be effective from July 1, 2010.
2. These have been placed before Federal and certain Provincial Parliaments, whilst will shortly be placed before the remaining Parliaments.
3. VAT will be applicable effectively on all Economic activities. Covering all ‘Supply of Goods’ and ‘Rendering of Services’. Very limited exceptions.
4. Present Sales Tax Act, 1990 and Five Provincial / Federal Capital Sales Tax Ordinances will be repealed.

A. VAT Implementation Plan – II

5. Federal Excise Duty to be realigned and streamlined so far as SERVICES are concerned.
6. Levy of taxes on ‘Goods’ by Federation and ‘Services’ by Provinces. Collection of tax on Services by the Federal Government as well. This is the basis of the present and proposed laws.
7. However, the principle agreed in NFC award [on December 11, 2009] i.e. Collection of VAT on Services by Provinces need to be resolved.

B. Economic Significance of VAT

1. Pakistan is struck up at less than 10% Tax to GDP ratio.
2. At least 7.5% growth is essential for our long-term economic survival.
3. This requires Broad-based consumption taxes.
4. Proper VAT, can add around Rs 800 to 1500 billion over a period of 3 to 5 years. Budget for 2009-10 is 499.4 billion for Sales Tax.
5. The above amount will be shared by us and accordingly, our Budgets need revision for the period from July 1, 2010.

سازِ الم نہ چھڑے، نوحہ غم نہ گائے
دل پہ نہ بوجھ لیجیے جان نہ یوں گھلایے
شامِ الم گھنی سہی ایک دیا جلایے
میری طرح سے دیکھیے گوشہٴ لب ہلایے

آپ بھی مسکرائے!

میری تو گل متاعِ زیست ہیں یہی مسکراہٹیں
ان سے ملی ہیں راحتیں، ان سے بھریں جراتیں
ان سے سچی رہیں سدا قلب و نظر میں جنتیں
سحرِ تبسم ایک بار آپ بھی آزمائے
آپ بھی مسکرائے!

C. Salient features – Federal VAT

- Standard rate of 15% has been proposed instead of existing standard rate of 16%.

- There would be **NO** –
 - Reduced tax
 - Enhanced tax
 - Special tax scheme/Special Procedure Rules
 - Retail price based tax

Retail Price

There is no concept of tax on Retail Price basis as per the draft VAT. Consequently, 17 items presently subject to ST on Retail Price as per the Third Schedule to ST will be chargeable to tax at standard rate of 15% of value of supply.

Exemptions

1. VAT has significantly reduced the quantum of Exemptions from about 465 to only 14 categories.
2. ST empowers the FBR to issue Exemption notifications and orders.
3. VAT provides that all Exempt goods shall be expressly provided only in Act and not elsewhere i.e. 14 categories.

Zero-rated Supplies

As per VAT, supply or import of the following types of items are Zero-rated:

- (a) Second Schedule to the Federal VAT
- (b) Zero-rated items under Provincial VAT
- (c) Supply of goods subject to certain conditions

These have been covered in the next few slides.

(a) Second Schedule - Zero-rated items

1. Sale or transfer of an economic activity, or part thereof, as a going concern
2. Supply of stores and provisions for consumption aboard
3. Such basic Pharmaceutical and Medical supplies as are specified by the FBR
4. A supply of precious metals

(b) Zero-rated items as per Prov. VAT

- 1. Services performed on goods outside Pakistan**
- 2. Leased goods outside Pakistan**
- 3. Services connected with Temporary Imports**
- 4. Services consumed outside Pakistan**

**(c) Zero-rated items Supply of goods -
Subject to certain conditions**

- 1. Export of goods**
- 2. Supply to Tourist or Visitor from Duty-free shops**
- 3. Supply for repairing, maintaining, cleaning, renovating, modifying, treating, or otherwise physically affecting other goods**
- 4. Supply relating to repair or replacement under Warranty**

Remaining Zero-rated items

1. No supply, class of supplies, import, or class of imports shall be treated as zero-rated except as expressly provided in Federal VAT
2. More than 200 categories notified through 16 SROs will be out of zero-rated regime, once the VAT Acts are enacted

New Terminologies Introduced in VAT

Increasing adjustments

Those tax issues which increase the tax liability of a person in addition to adjustment on account of output tax.

Decreasing adjustments

Such tax issues which decrease the tax liability of a person in addition to adjustment on account of input tax.

New terms introduced in VAT

Economic Activity

The term 'Economic Activity' has been used in VAT as against the term 'Taxable Activity' used in ST.

Entertainment

It means the provision of food, beverages, tobacco, amusement, recreation, or hospitality of any kind, whether or not the provision of such entertainment is lawful.

Federal List Services

ST Act only covers taxability of goods; whereas ST on services is covered under Provincial ST Ordinances. As per Federal VAT bill, Services on account of Carriage of Goods or Passengers by way of Railway, Sea or Air will be subjected to Federal VAT.

Other new terms

Sr. No.	Terminologies
1	Ancillary or incidental supplies
2	Approved non-profit charitable organization
3	Creditable purpose
4	Consideration
5	Imposed (charged, levied and payable)
6	International transport
7	Money
8	Permanent establishment

Other new terms

Sr. No.	Terminologies
9	Passenger vehicle
10	Private purpose use
11	Progressive/periodic supply
12	Recipient
13	Registration threshold
14	Resident/non-resident person
15	Second-hand goods
16	Sale receipts

Bad Debts – Decreasing Adjustment/Input allowable

1. VAT comprehensively specifies the procedure to be followed if all or part of the consideration has not been paid to the supplier.
2. It allows the supplier to make a decreasing adjustment and vice versa adjustment for purchaser.

Advance tax

1. VAT empowers FBR to specify ANY person or class of person to pay advance tax upto 25% of the Standard rate (i.e. effectively 3.75% of Value of Supply) as Prospective Value additions.
2. In ST, the FBR has specified 2% Minimum Value additions at 2 % ONLY for Importers.

Withholding tax by Government & LTU Taxpayers

1. VAT empowers the FBR to specify tax to withheld by ANY purchaser of goods upto 25% (i.e. effectively 3.75% of Value of Supply).
- 2 As per ST, the FBR has specified certain Government Departments and bodies to withhold ST @ 3.2% of the value of supply. Moreover, the recipients of Advertisement services are presently required to withhold ST @ 16 %.

Revised Return

1. As per ST, a revised return can be filed within 120 days, after the approval of the Commissioner.
2. Pursuant to VAT, application for the revised return can be made within 3 years but to the FBR rather than Commissioner.

Authorisation for Recovery of Arrears

The Officer of Inland Revenue will have to obtain authorization from the FBR or Commissioner before starting the recovery proceedings as per VAT. Presently, the Officer is independent in this regard.

Powers of FBR & Commissioner to Re-open cases

As per VAT, the FBR and Commissioner have been empowered to examine the record (to re-open) even if the appeal is pending before the Commissioner – Appeals. No such powers exist in ST.

Appeal to Appellate Tribunal

1. As per VAT, the Additional Commissioner has to obtain authorization from the Commissioner before filing an appeal before the Appellate Tribunal.
2. Pursuant to ST, the AC was independent in this regard.

Powers to make VAT Rules

1. The VAT Rules made during a year by the FBR will be placed before the National Assembly alongwith the budget every year.
2. Books publication, as per ST, will be done away with, as moving forward towards the Paper-Less offices.

Repeal and Savings

1. It is being published in the newspapers that Provincial VAT Acts will replace Provincial Ordinances as well as Federal Excise Duty on Services.
2. Section 95 of Federal VAT Bill will repeal by the ST Act. Provincial VAT will repeal Provincial Ordinances.
3. Federal VAT is silent as to repeal of the Services covered under the Federal Excise Act.

Certain Restriction in ST on input tax adjustments [ST 8B(1)] – Eliminated from VAT

The following restrictions & conditions for adjustment and refund of input tax provided in ST have been eliminated.

1. Adjustment and refund upto 90% of output
2. Adjustment of tax paid on acquisition of Fixed assets in 12 Monthly installments

No Powers to Postpone Refund Payment

As per ST, the Refund payment can be postponed by the Tax Department until the disposal of appeal by the Supreme Court. No such provision exist in VAT, as such, beneficial to the taxpayers.

D. Salient features - Draft Prov. VAT Acts VS Applicable Prov. Ordinances

Presently applicable Provincial ST Ordinances specify that ONLY the following 4 Services Categories are taxable:

- 1. Hotels, Marriage Halls, Lawns, Clubs and Caterers**
- 2. Advertisement on TV and Radio**
- 3. Customs Agents, Ship Chandlers and Stevedores**
- 4. Courier**

On the other hand, Draft Provincial VAT Act specify that ALL the Services are taxable except for 6 Categories listed in the 1st Schedule.

Service Nature And Exempt Services

Service has been very widely defined as “anything that is not goods, immovable property or money”. As such, ALL types of Services are taxable, except the following:

1. Funeral, burial or similar services
2. Services by religious institutions
3. Services by an approved non-profit charitable organization
4. Certain Financial services.
5. Certain education services provided by an institution duly registered by the Minister of Education
6. Certain supplies of immovable property

E. Implementation Issues – I

1. **GST, on Wholesale & Retail Trades, has not been successful. As such, almost the whole sector is outside the GST net at present.**
2. **Implementation has failed on account of both policy and administrative issues as well as lack of Good Governance coupled with Corruption.**

E. Implementation Issues – II

3. Income tax provisions promoting Final Tax Regime
4. Under invoicing and Flying invoice
5. Smuggled and abuse of Afghan Transit Trade
6. Goods originating from informal and undocumented sector



F. Administrative Actions planned / in Progress to implement VAT

- 1. Three new RTOs are being established; One for Lahore & Two for Karachi.**
- 2. Sindh Revenue Service (SRS) Department is being established.**
- 3. In LTU Karachi, one Commissioner Audit & several officers have already been added.**



WAY FORWARD

G. Way Forward – I

1. **Proper communication with all the Stakeholders. Even the tax rate on Services is not known so far. Draft Rules and certain SROs yet to be circulated.**
2. **Political & Social consensus and its acceptability. Serious efforts for Good Governance.**
3. **Action against Undocumented Economy, Under Invoicing, Flying Invoicing, Smuggling, Abuse of ATT and Corruption.**

Otherwise, Honest will pay more and Others will enjoy as usual.

*"When there is a tax,
the just man will pay
more and the unjust
less, on the same
actions."*

PLATO

G. Way Forward – II

4. Creation of National and Industry specific data and information on transparent basis.
5. Downward revision of the rate of Federal VAT from 15% to Say 10% to make it acceptable. Provincial VAT is recommended at 5%.
6. Abolition of FTR in income tax.
7. Full day Seminars and two-three days Workshops prior to its implementation.

8. Group Discussions.



"Taxes, after all, are dues that we pay for the privileges of Membership in an Organised Society."

Franklin D. Roosevelt - 1936



THANK YOU